



**SECURITIES AND EXCHANGE COMMISSION**

**[Release No. 34-93122; File No. SR-CBOE-2021-041]**

**Self-Regulatory Organizations; Cboe Exchange, Inc.; Order Granting Approval of a Proposed Rule Change, as Modified by Amendment No. 2, to Amend Certain Rules to Accommodate the Listing and Trading of Micro FLEX Index Options and to Make Other Clarifying and Non-substantive Changes**

September 24, 2021.

On July 23, 2021, Cboe Exchange, Inc. (“Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to accommodate the listing and trading of flexible exchange (“FLEX”) index options with an index multiplier of one (“Micro FLEX Index Options”) and to make other clarifying and non-substantive changes.<sup>3</sup> The proposed rule change was published in the Federal Register on August 12, 2021.<sup>4</sup> On September 22, 2021, the Exchange submitted partial Amendment No. 2 to the proposed rule change.<sup>5</sup> The Commission received no comments on the proposed rule change. The Commission is approving the proposed rule change, as modified by Amendment No. 2.

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> On August 4, 2021, the Exchange filed partial Amendment No. 1 to the proposed rule change. The Exchange withdrew partial Amendment No. 1 on August 6, 2021.

<sup>4</sup> Securities Exchange Release No. 92599 (August 6, 2021), 86 FR 44411 (August 12, 2021) (“Notice”).

<sup>5</sup> In Amendment No. 2, the Exchange stated that, currently, the Exchange lists non-FLEX options on 12 (not 13, as stated in the Exchange’s original filing) broad-based indexes with a value of at least 100, and the proposed rule change would authorize the Exchange to list Micro FLEX Options on the same 12 indexes, which are all broad-based and all have a value of at least 100. The Exchange stated that it delisted options on FTSE 100 Mini-Index (UKXM). The Exchange also made a conforming change to its representation under the heading “Capacity.” Because Amendment No. 2 does not materially alter the substance of the proposed rule change, Amendment No. 2 is not subject to notice and comment. Amendment No. 2 is available on the Commission’s website at: <https://www.sec.gov/comments/sr-cboe-2021-041/srcboe2021041.htm>.

I. Description of the Proposed Rule Change, as Modified by Amendment No. 2

The Exchange proposes to amend its rules to permit the trading of FLEX index options with an index multiplier of one on broad-based indexes for which the value of the underlying is at least 100. The Commission recently approved a rule change that provided the Exchange with the authority to list options with an index multiplier of one on broad-based indexes for which the value of the underlying is at least 100 on the Exchange's standardized, non-FLEX market.<sup>6</sup>

Currently, CBOE Rule 4.21(b)(1) states the index multiplier for FLEX index options is 100. The Exchange proposes to add to the rule that the index multiplier for FLEX index options on broad-based indexes for which the value of the underlying is at least 100<sup>7</sup> may also be one in addition to the current index multiplier of 100. The proposed rule change amends CBOE Rule

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<sup>6</sup> See CBOE Rule 4.11 (providing for the listing of non-FLEX options with a multiplier of one ("micro-options")). See Securities Exchange Release No. 91528 (April 9, 2021), 86 FR 19933 (April 15, 2021). According to the Exchange, currently, the Exchange lists non-FLEX options on 12 broad-based indexes with a value of at least 100: S&P 500 Index, Mini-S&P 500 Index (XSP), Russell 2000 Index (RUT), Mini-Russell 2000 Index (MRUT), Dow Jones Industrial Average (DJX), S&P 100 Index (OEX and XEO), S&P 500 ESG Index (SPESG), MSCI EAFE Index (MXEA), MSCI Emerging Markets Index (MXEF), Russell 1000 Growth Index (RLG), Russell 1000 Value Index (RLV), and Russell 1000 Index (RUI). The Exchange states that the proposed rule change will authorize the Exchange to list Micro FLEX Index Options on the same 12 indexes, which are all broad-based and all have a value of at least 100. In Amendment No. 2, the Exchange stated that it may authorize for trading a FLEX option class on any index if it may authorize for trading a non-FLEX option class on that index, even if the Exchange does not list that non-FLEX option class for trading. Currently, the Exchange is authorized to (but does not) list for trading options on six additional broad-based indexes with values of at least 100. The Exchange stated that the Exchange's system currently prevents FLEX trading on these indexes (and other underlying securities and indexes on which the Exchange does not list non-FLEX options even though authorized to under its rules). If the Exchange updates its system in the future to permit FLEX trading on underlying securities or indexes on which the Exchange does not list non-FLEX options, Micro FLEX Index Options on these six indexes (assuming they still satisfied the Exchange's maintenance listing criteria in Rule 4.10 and had values of at least 100) would be permitted to be listed and traded. See *infra* note 27.

<sup>7</sup> These are the same indexes on which the Exchange may list micro-options.

4.21(b)(1) to state that if a FLEX Trader<sup>8</sup> specifies an index on a FLEX Order,<sup>9</sup> the FLEX Trader must also include whether the index option has an index multiplier of 100 or 1 when identifying the class of FLEX Order.<sup>10</sup> The Exchange states that, to the extent the Exchange lists a Micro FLEX Index Option on an index on which it also lists a standard FLEX index option, it will be listed with a different trading symbol than the standard index option with the same underlying index to reduce any potential confusion.<sup>11</sup>

In its proposal, the Exchange stated that its rules permit trading in a put or call FLEX option series only if it does not have the same exercise style, same expiration date, and same exercise price as a non-FLEX option series on the same underlying security or index that is already available for trading.<sup>12</sup> The Exchange proposes to add to the introductory paragraph of CBOE Rule 4.21(b) that a FLEX index option with an index multiplier of one may not be the same type (put or call) and may not have the same exercise style, expiration date, settlement type, and exercise price as a non-FLEX index option overlying the same index listed for trading (regardless of the whether the index multiplier of the non-FLEX index option is one or 100). As

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<sup>8</sup> A “FLEX Trader” is a Trading Permit Holder the Exchange has approved to trade FLEX options on the Exchange.

<sup>9</sup> A “FLEX Order” is an order submitted in FLEX options. The submission of a FLEX Order makes the FLEX option series in that order eligible for trading. See CBOE Rule 5.72(b).

<sup>10</sup> When submitting a FLEX Order, the submitting FLEX Trader must include all required terms of a FLEX option series. These terms include, in addition to the underlying equity security or index, the type of options (put or call), exercise style, expiration date, settlement type, and exercise price. See CBOE Rule 4.21(b). Pursuant to CBOE Rule 4.21(b)(1), the submitting FLEX Trader must include the underlying equity security or index on the FLEX Order. The Exchange states that, therefore, each FLEX index option series in a Micro FLEX Index Option class will include the same flexible terms as any other FLEX option series, including strike price, settlement, expiration date, and exercise style as required by CBOE Rule 4.21(b).

<sup>11</sup> The Exchange states that, for example, a standard FLEX index option for index ABC with an index multiplier of 100 may have symbol 4ABC, while a Micro FLEX Index Option for index ABC with a multiplier of one may have symbol 4ABC9 and a non-FLEX option on index ABC with an index multiplier of 100 may have symbol ABC, while a non-FLEX micro-option would have a different symbol (such as ABC9).

<sup>12</sup> See CBOE Rule 4.21(a)(1).

a result, a Micro FLEX Index Option may not have the same terms as a non-FLEX index option or non-FLEX micro-option. The Exchange states that this will prevent a Micro FLEX Index Option from being listed with terms identical to those of a non-FLEX index option with a multiplier of 100 or a non-FLEX micro-option with a multiplier of one on the same index.

The Exchange states that a Micro FLEX Index Option would become fungible<sup>13</sup> with a non-FLEX micro-option with the same terms pursuant to CBOE Rule 4.22(a), but would not be fungible with a non-FLEX option overlying the same index with a multiplier of 100 with the same expiration date, settlement, and exercise price. The Exchange states that because the proposed rule change would not permit a Micro FLEX Index Option to be listed with the same terms as a non-FLEX index option regardless of the index multiplier, proposed CBOE Rule 4.22(b)(2) will provide that if a non-FLEX index option series with an index multiplier of 100 and the same terms as a Micro FLEX Index Option overlying the same index is listed for trading, a position established under the FLEX trading procedures may be closed using the FLEX trading procedures in Chapter 5, Section F against another closing only FLEX position during the time period that non-FLEX index option series is listed for trading. During the time that non-FLEX index option series is listed for trading, pursuant to CBOE Rule 5.72, no FLEX Orders may be submitted into an electronic auction or represented for open outcry trading for a FLEX index option series with a multiplier of one with the same terms as the non-FLEX index option series overlying the same index with an index multiplier of 100, unless the FLEX Order is a closing order.<sup>14</sup> This proposed “closing only” process is similar to the current “closing only” process for non-FLEX option American-style series added intraday, as set forth in current CBOE Rule

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<sup>13</sup> Under CBOE Rule 4.22(a), if the Exchange lists for trading a non-FLEX option series with identical terms as a FLEX option series, all existing open positions established under the FLEX trading procedures are fully fungible with the non-FLEX option series, and any further trading in the series would be as non-FLEX options subject to non-FLEX trading procedures and rules.

<sup>14</sup> The Exchange states that, to the extent the non-FLEX index option is later delisted, then opening trades of the Micro FLEX Index Option may resume after that occurs.

4.22(b).<sup>15</sup> The Exchange states that this proposed change would prevent new Micro FLEX Index Option positions from being opened when a non-FLEX Index Option with a multiplier of 100 with the same terms is listed for trading.<sup>16</sup> In addition, as proposed, CBOE Rule 4.22(b) would require that the Exchange notifies FLEX Traders when a FLEX option series is restricted to closing only transactions.<sup>17</sup>

### Trading Hours

Pursuant to CBOE Rule 5.1(b)(3)(A) and (c)(1), Micro FLEX Index Options will be available for trading during the same hours as non-FLEX Index Options pursuant to CBOE Rule 5.1(b)(2). Accordingly, Regular Trading Hours for Micro FLEX Index Options will generally be 9:30 a.m. to 4:15 p.m. Eastern time.<sup>18</sup> To the extent an index option is authorized for trading during Global Trading Hours, the Exchange states it may also list Micro FLEX Index Options during that trading session as well, the hours for which trading session are 3:00 a.m. to 9:15 a.m. Eastern time.

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<sup>15</sup> The Exchange plans to renumber current CBOE Rule 4.22(b) as CBOE Rule 4.22(b)(1), accompanied by non-substantive punctuation mark changes to reflect proposed CBOE Rule 4.22(b)(2).

<sup>16</sup> As proposed, if the Exchange lists a non-FLEX index option with a multiplier of one with identical terms as a Micro FLEX Index Option, then current CBOE Rule 4.22(a) applies to the fungibility of those options (or proposed CBOE Rule 4.22(b)(1) if it is an American-style series added intraday) and the FLEX Micro Index Option would no longer be a FLEX option, but instead be traded as a standard micro-option.

<sup>17</sup> The Exchange proposes to move this provision to make it clear it will apply to the entire paragraph (b) as proposed to be amended, and to make changes that it states would modernize this provision. Currently, CBOE Rule 4.22(b) states that a FLEX Official announces to FLEX Traders when such a FLEX option series is restricted to closing only transactions. The Exchange states that this was true when FLEX options were traded only in open outcry and a verbal announcement was made to the trading floor. The Exchange states that currently, because FLEX options are available for electronic and open outcry trading, the Exchange notifies FLEX Traders when a FLEX option series is restricted to closing only transactions. Accordingly, the Exchange proposes to revise Rule 4.22(b) to state that the Exchange notifies FLEX Traders when a FLEX Option series is restricted to closing only transactions. The Exchange also states that, in accordance with CBOE Rule 1.5, the Exchange currently notifies FLEX Traders of restricted FLEX option series by electronic message.

<sup>18</sup> Certain indexes close trading at 4:00 p.m. Eastern time. See CBOE Rule 5.1.

### Expiration, Settlement, and Exercise Style

In accordance with CBOE Rule 4.21(b), FLEX Traders may designate the type (put or call), exercise style, expiration date, and settlement type of Micro FLEX Index Options.

### Exercise Prices

The Exchange proposes to amend CBOE Rule 4.21(b)(6) to state that the exercise price for a FLEX index option series in a class with a multiplier of one is set at the same level as the exercise price for a FLEX index option series in a class with a multiplier of 100. To illustrate the deliverable exercise price for index options with different multipliers as well as physically settled equity options, the proposed rule change adds the following examples to CBOE Rule 4.21(b)(6) regarding how the deliverable for a Micro FLEX Index Option will be calculated (as well as for a FLEX index option with a multiplier of 100 and a FLEX equity option, for additional clarity and transparency): If the exercise price of a FLEX option series is a fixed price of \$50, it will deliver: (A) 100 shares of the underlying security at \$50 (with a total deliverable of \$5,000) if a FLEX equity option; (B) cash equal to 100 (i.e., the index multiplier) times 50 (with a total deliverable value of \$5,000) if a FLEX index option with a multiplier of 100; and (C) cash equal to 1 (i.e., the index multiplier) times 50 (with a total deliverable value of \$50) if a Micro FLEX Index Option. If the exercise price of a FLEX option series is 50% of the closing value of the underlying security or index, as applicable, on the trade date, it will deliver: (A) 100 shares of the underlying security at a price equal to 50% of the closing value of the underlying security on the trade date (with a total deliverable of 100 times that percentage amount) if a FLEX Equity Option; (B) cash equal to 100 (i.e., the index multiplier) times a value equal to 50% of the closing value of the underlying index on the trade date (with a total deliverable of 100 times that percentage amount) if a FLEX index option with a multiplier of 100; and (C) cash equal to 1 (i.e., the index multiplier) times a value equal to 50% of the closing value of the underlying index on the trade date (with a total deliverable of one times that percentage amount) if a Micro FLEX Index Option. The Exchange states that the descriptions of exercise prices for FLEX

equity options and FLEX index options with a multiplier of 100 are true today, and that the examples merely add clarity to the rules.

### Bids and Offers

Pursuant to CBOE Rule 5.4(c), the Exchange states that it will determine the minimum increment for bids and offers on Micro FLEX Index Options (as it does for all other FLEX options) on a class-by-class basis, which may not be smaller than (1) \$0.01, if the exercise price for the FLEX option series is a fixed price, or (2) 0.01%, if the exercise price for the FLEX option series is a percentage of the closing value of the underlying equity security or index on the trade date.<sup>19</sup> The proposed rule change amends CBOE Rule 5.3(e)(3) to describe the difference between the expression of bids and offers for FLEX equity options, FLEX index options with a multiplier of 100, and Micro FLEX Index Options. Currently, that rule states that bids and offers for FLEX options must be expressed in (a) U.S. dollars and decimals if the exercise price for the FLEX option series is a fixed price, or (b) a percentage, if the exercise price for the FLEX option series is a percentage of the closing value of the underlying equity security or index on the trade date, per unit.<sup>20</sup> As noted above, a FLEX option contract unit consists of 100 shares of the underlying security or 100 times the value of the underlying index, as they currently have a 100 contract multiplier.<sup>21</sup>

The proposed rule change states that bids and offers for Micro FLEX Index Options must be expressed in (a) U.S. dollars and decimals if the exercise price for the FLEX option series is a

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<sup>19</sup> The System (as defined in CBOE Rule 1.5(aa)) rounds bids and offers to the nearest minimum increment.

<sup>20</sup> The Exchange states that the proposed rule change reorganizes the language in this provision to make clear that the phrase “if the exercise price for the FLEX option series is a percentage of the closing value of the underlying equity security or index on the trade date” applies to the entire clause (B) of 5.3(e)(3). The proposed rule change also adds a cross-reference to CBOE Rule 5.4 to provide that bids and offers in U.S. dollars and decimals and percentages of the closing values of the underlying equity security or index on the trade date must be in the applicable minimum increment as set forth in CBOE Rule 5.4.

<sup>21</sup> See current CBOE Rule 4.21(b)(1).

fixed price, or (b) a percentage per unit (if a FLEX equity option or a FLEX index option with a multiplier of 100) or per 1/100<sup>th</sup> unit (if a FLEX index option with a multiplier of one) of the underlying security or index, as applicable, if the exercise price for the FLEX option series is a percentage of the closing value of the underlying equity security or index on the trade date. Additionally, the proposed rule change adds examples describing how FLEX options bids and offers must be expressed. The proposed rule will state that, if the exercise price of a FLEX option series is a fixed price, a bid of “0.50” represents a bid of (A) \$50 (0.50 times 100 shares) for a FLEX equity option; (B) \$50 (0.50 times an index multiplier of 100) for a FLEX index option with a multiplier of 100; and (C) \$0.50 (0.50 times an index multiplier of one) for a Micro FLEX Index Option. If the exercise price of a FLEX option series is a percentage of the closing value of the underlying equity security, a bid of “0.50” represents a bid of (A) 50% (0.50 times 100 shares) of the closing value of the underlying equity security on the trade date if a FLEX equity option; (B) 50% (0.50 times an index multiplier of 100) of the closing value of the underlying index on the trade date if a FLEX index option with a multiplier of 100; and (C) 0.50% (0.50 times an index multiplier of one) of the closing value of the underlying index on the trade date if a Micro FLEX Index Option. The Exchange states that it believes the proposed rule language identifies a clear, transparent description of the differences between FLEX index options with a multiplier of 100 and Micro FLEX Index Options and provides clarity regarding how bids and offers of FLEX equity options and FLEX index options with a multiplier of 100 will be required to be expressed.

#### Contract Size Limits

The Exchange states that the proposed rule change updates various other provisions in the following rules to reflect that 100 Micro FLEX Index Options overlying an index will be economically equivalent to one contract for a standard index option overlying the same index:

- Rule 5.74: CBOE Rule 5.74 describes the Exchange’s FLEX Solicitation Auction Mechanism (“FLEX SAM”). An order, or the smallest leg of a complex order, must be



for at least the minimum size designated by the Exchange (which may not be less than 500 standard option contracts or 5,000 mini-option contracts). The proposed rule change adds that 50,000 Micro FLEX Index Options is the corresponding minimum size for orders submitted into FLEX SAM Auctions.

- Rule 5.87: CBOE Rule 5.87(f) describes when a Floor Broker is entitled to cross a certain percentage of an order, subject to the requirements in that paragraph. Under that rule, the Exchange may determine on a class-by-class basis the eligible size for an order that may be transacted pursuant to that paragraph; however, the eligible order size may not be less than 50 standard option contracts (or 500 mini-option contracts or 5,000 for micro-options). The proposed rule change adds that 5,000 FLEX index option contracts with an index multiplier of one is the corresponding minimum size for orders that may be crossed in accordance with this provision. Additionally, CBOE Rule 5.87, Interpretation and Policy .07(a) provides that CBOE Rule 5.86(e)<sup>22</sup> does not prohibit a Trading Permit Holder (“TPH”) from buying or selling a stock, security futures or futures position following receipt of an order, including an option order, but prior to announcing such order to the trading crowd, provided that the option order is in a class designated as eligible for “tied hedge” transactions and within the eligibility size parameters, which are

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<sup>22</sup> The Exchange states that CBOE Rule 5.86(e) provides that it will be considered conduct inconsistent with just and equitable principles of trade for any TPH or person associated with a TPH, who has knowledge of all material terms and conditions of an original order and a solicited order, including a facilitation order, that matches the original order’s limit, the execution of which are imminent, to enter, based on such knowledge, an order to buy or sell an option of the same class as an option that is the subject of the original order, or an order to buy or sell the security underlying such class, or an order to buy or sell any related instrument until either (1) all the terms and conditions of the original order and any changes in the terms and conditions of the original order of which that TPH or associated person has knowledge are disclosed to the trading crowd or (2) the solicited trade can no longer reasonably be considered imminent in view of the passage of time since the solicitation. An order to buy or sell a “related instrument,” means, in reference to an index option, an order to buy or sell securities comprising ten percent or more of the component securities in the index or an order to buy or sell a futures contract on any economically equivalent index.

determined by the Exchange and may not be smaller than 500 standard option contracts (or 5,000 mini-option contracts or 50,000 micro-options). The proposed rule change adds that 50,000 FLEX index option contracts with a multiplier of one is the corresponding minimum size for orders that may qualify as tied hedge transactions and not be deemed a violation of CBOE Rule 5.86(e).

#### Position and Exercise Limits<sup>23</sup>

The proposed rule change amends CBOE Rule 8.35(a) regarding position limits for FLEX options to describe how Micro FLEX Index Options will be counted for purposes of determining compliance with position limits.<sup>24</sup> Because 100 Micro FLEX Index Options are equivalent to one FLEX index option with a multiplier of 100 overlying the same index due to the difference in contract multipliers, proposed CBOE Rule 8.35(a)(7) states that for purposes of determining compliance with the position limits under CBOE Rule 8.35, 100 Micro FLEX Index Option contracts equal one FLEX index option contract with a multiplier of 100 with the same underlying index. The proposed rule change makes a corresponding change to CBOE Rule 8.35(b) to clarify that, like reduced-value FLEX contracts, Micro FLEX Index Option contracts will be aggregated with full-value contracts and counted by the amount by which they equal a full-value contract for purposes of the reporting obligation in that provision (*i.e.*, 100 Micro FLEX Index Options will equal one FLEX index option contract with a multiplier of 100 overlying the same index).<sup>25</sup> The proposed rule change also adds that Micro FLEX Index

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<sup>23</sup> The Exchange states that, to the extent the Exchange lists Micro FLEX Index Options on other indexes in the future, they would be subject to the same position and exercise limits set forth in the applicable rules, and similarly aggregated with standard options on the same indexes, as proposed.

<sup>24</sup> The proposed rule change also corrects an administrative error in CBOE Rule 8.35(a). Currently, there are two subparagraphs numbered as (a)(5). The proposed rule change amends paragraph (a) to renumber the second subparagraph (a)(5) to be subparagraph (a)(6).

<sup>25</sup> The Exchange states that, as it does today with respect to reduced-value indexes, the Exchange will count Micro FLEX Index Options as a percentage of a FLEX index option with a multiplier of 100 when calculating positions to determine compliance with

Options on certain broad-based indexes for which FLEX index options with a multiplier of 100 have no position limits will also have no position limits. The proposed rule change amends CBOE Rule 8.42(g) to make corresponding changes regarding the application of exercise limits to Micro FLEX Index Options. This is consistent with the current treatment of other reduced-value FLEX index options with respect to position and exercise limits. The margin requirements set forth in Chapter 10 of the Exchange's Rules will apply to Micro FLEX Index Options (as they currently do to all FLEX options).<sup>26</sup>

#### Capacity

The Exchange represents that it believes the Exchange and Options Price Reporting Authority ("OPRA") have the necessary systems capacity to handle the additional traffic associated with the listing of new series that may result from the introduction of the Micro FLEX Index Options. Because the proposed rule change is limited to broad-based index options, which currently represent only 12 of the indexes on which the Exchange listed on the Exchange, the Exchange states that believes any additional traffic that may be generated from the introduction of Micro FLEX Index Options will be manageable.<sup>27</sup> The Exchange states that it also understands that the OCC will be able to accommodate the listing and trading of Micro FLEX Index Options.

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position limits.

<sup>26</sup> According to the Exchange, pursuant to CBOE Rule 8.43(j), FLEX index options with a multiplier of one will be aggregated with non-FLEX index options on the same underlying index in the same manner as all other FLEX index options.

<sup>27</sup> The Exchange states that if it updates its system to permit FLEX trading on underlying securities and indexes on which it does not list non-FLEX options, including Micro FLEX Index Options trading on broad-based indexes with a value of at least 100, the Exchange would do so only if it had sufficient capacity to permit such additional trading. See supra note 6.

## Other Changes

The Exchange proposes to amend CBOE Rule 4.21(b)(6) to state that the exercise price may be in increments no smaller than:<sup>28</sup> (1) for a FLEX equity option or FLEX index option that is not Cliquet-settled, (a) \$0.01, if the exercise price for the FLEX option series is expressed as a fixed price in terms of dollars and decimals or a specific index value, as applicable, or (b) 0.01%, if the exercise price for the FLEX option series is expressed as a percentage of the closing value of the underlying equity security or index on the trade date, as applicable. The proposed rule change also adds to CBOE Rule 4.21(b)(6) after subparagraph (B) that the Exchange may determine the smallest increment for exercise prices of FLEX options on a class-by-class basis. The Exchange states that these changes codify long-standing interpretations of the current rule, which references the minimum increment for bids and offers as set forth in CBOE Rule 5.4.<sup>29</sup> The Exchange states that it believes this will make the rule regarding permissible exercise prices for FLEX options more transparent and thus may eliminate potential confusion regarding permissible exercise prices.<sup>30</sup>

The proposed rule change moves the parenthetical regarding the system rounding the exercise price to the nearest minimum increment for bids and offers in the class (as set forth in CBOE Rule 5.4) from the introductory clause in CBOE Rule 4.21(b)(6) to the end of subclause (A)(ii) so that it applies only to that subclause, as rounding would only apply to exercise prices expressed as a percentage. The proposed rule change also adds to the parenthetical in CBOE Rule 4.21(b)(6)(A)(ii) that the system rounds the “actual” exercise price to the nearest fixed price

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<sup>28</sup> The Exchange states that this language is taken from CBOE Rule 5.4(c)(4).

<sup>29</sup> The Exchange states that the proposed rule change makes non-substantive changes to the structure of this sentence to accommodate the addition of the specific minimum increments for the exercise price.

<sup>30</sup> The Exchange also states that it believes flexibility for the Exchange to determine the smallest increment for exercise prices of FLEX options on a class-by-class basis is appropriate to permit the Exchange to make determinations based on the market characteristics of different classes. The Exchange notes the rules of another options exchange similarly permit that exchange to determine on a class-by-class basis both minimum increments for exercise prices and premiums (*i.e.*, bids and offers) stated using a percentage-based methodology. *See, e.g.*, NYSE Arca, Inc. Rule 5.32-O(e)(2)(C).

minimum increment to provide additional clarity to the provision, as the dollar value of an exercise price expressed as a percentage determined after the closing value is available would be rounded to the nearest minimum dollar value increment, which dollar value would represent the ultimate, “actual” exercise price.

In addition, the proposed rule change clarifies in CBOE Rule 5.3(e)(3) and 5.4(c)(4) that, following application of the designated percentage to the closing value of the underlying security or index, the system rounds the final transaction prices (rather than bids and offers) of FLEX options to the nearest fixed price minimum increment for the class as set forth in CBOE Rule 5.4(c)(4)(A). The Exchange states that this is consistent with current functionality and is merely a clarification in the CBOE Rules to more accurately reflect how the System currently works.

In addition, the Exchange proposes to add a parenthetical in the first paragraph of CBOE Rule 5.3(e)(3)(B) to state that bids and offers would be in the applicable minimum increment as set forth in CBOE Rule 5.4. The Exchange states that this is true today and merely incorporates a cross-reference to CBOE Rule 5.4, which describes permissible minimum increments for bids and offers. The Exchange states that it believes the addition of this cross-reference will provide additional transparency and clarity to this rule.

The proposed rule change also codifies in CBOE Rules 5.72(c)(3)(A) and (d)(2), 5.73(e), and 5.74(e) how FLEX Auction response bids and offers (as well as Initiating Orders<sup>31</sup> and Solicited Orders<sup>32</sup> with respect to FLEX AIM Auctions and FLEX SAM Auctions, respectively) are ranked during the allocation process following each type of FLEX Auction (i.e., electronic FLEX Auction, open outcry FLEX Auction, FLEX AIM Auction, and FLEX SAM Auction, respectively). The Exchange states that FLEX Orders will always first be allocated to responses at the best price, as

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<sup>31</sup> “Initiating Order” is defined in CBOE Rule 5.37.

<sup>32</sup> “Solicited Order” is defined in CBOE Rule 5.39.

applicable.<sup>33</sup> The proposed rule change clarifies that the term “price” refers to (1) the dollar and decimal amount of the order or response bid or offer or (2) the percentage value of the order or response bid or offer, as applicable. The Exchange states that these are non-substantive changes, as they reflect how ranking following FLEX Auctions occurs today, and the Exchange believes these changes will provide additional transparency in the CBOE Rules.

Finally, in CBOE Rule 4.22(b), the proposed rule change modernizes the provision regarding how FLEX Traders are notified when a FLEX option series becomes restricted. The Exchange also proposes to move this provision to make it clear it will apply to the entire paragraph (b) as proposed to be amended. Currently, CBOE Rule 4.22(b) states a FLEX Official<sup>34</sup> announces to FLEX Traders when such a FLEX option series is restricted to closing only transactions. The Exchange states that this was true when FLEX options were traded only in open outcry and a verbal announcement was made to the trading floor. The Exchange states that currently, because FLEX options are available for electronic and open outcry trading, the Exchange notifies FLEX Traders when a FLEX option series is restricted to closing only transactions. In accordance with CBOE Rule 1.5, the Exchange currently notifies FLEX Traders of restricted FLEX option series by electronic message.

## II. Discussion and Commission Findings

After careful review of the proposal and the comments received, the Commission finds that the proposed rule change, as modified by Amendment No. 2, is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>35</sup> In particular,

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<sup>33</sup> The proposed rule change also clarifies this in CBOE Rule 5.72(d)(2) by adding a cross-reference to CBOE Rule 5.85(a)(1), which states that, with respect to open outcry trading on the Exchange’s trading floor, bids and offers with the highest bid and lowest offer have priority. This is a non-substantive change that is currently true for open outcry FLEX Auctions, and the proposed rule change merely makes this explicit in CBOE Rule 5.72(d)(2), which cross-reference was previously inadvertently omitted from the CBOE Rules.

<sup>34</sup> “FLEX Official” is defined in CBOE Rule 5.75.

<sup>35</sup> In approving this proposed rule change, as modified by Amendment No. 2, the

the Commission finds that the proposed rule change, as modified by Amendment No. 2, is consistent with Section 6(b)(5) of the Act,<sup>36</sup> which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.

The FLEX options market was designed to accommodate flexibility in setting the specific terms of an options contract for the purpose of satisfying particular investment objectives that could not be met by the Exchange's standardized non-FLEX options market.<sup>37</sup> By permitting traders to adjust the flexible terms (e.g., strike price, expiration date, and exercise style), market participants can trade customized options on the Exchange that are not available in the non-FLEX options market.<sup>38</sup> As discussed above, the Exchange may list options with an index multiplier of one on broad-based indexes for which the value of the underlying index is at least 100.<sup>39</sup> By permitting Micro FLEX Index Options on such indexes, the proposal will permit

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Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>36</sup> 15 U.S.C. 78f(b)(5).

<sup>37</sup> See Securities Exchange Act Release No. 31920 (February 24, 1993), 58 FR 12280 at 12281 (March 3, 1993) (original order approving a CBOE proposal to list and trade FLEX options on the S&P 100 and 500 Index options).

<sup>38</sup> The FLEX options market operates under a separate structure than the standardized non-FLEX options market ("non-FLEX options market") and does not offer the same level of transparency as the non-FLEX options market. Among the differences between the market structure for FLEX options and non-FLEX options is that the FLEX options market does not have a public customer order book and there is no national best bid or offer ("NBBO").

<sup>39</sup> See supra note 6.

FLEX Traders to customize the flexible terms of such options that are authorized for trading on the non-FLEX market.

In support of its proposal, the Exchange states that the proposed rule change will expand investor choice and flexibility.<sup>40</sup> In particular, the Exchange states that listing and trading of Micro FLEX Index Options could benefit investors by providing them additional granularity with respect to the prices at which they may execute and exercise index options on the Exchange.<sup>41</sup> The Exchange states that, in particular, it believes that Micro FLEX Index Options would provide institutional investors with an additional exchange-traded tool to manage the positions and associated risk in their portfolios more precisely based on notional value, which currently may equal a fraction of a standard contract.<sup>42</sup> The Exchange states that, given the various trading and hedging strategies employed by investors, this additional granularity may provide investors with more control over the trading of their investment strategies and management of their positions and risk associated with option positions in their portfolios.<sup>43</sup> The Exchange further states that this flexibility is currently available on the OTC market, and believes that the proposed rule change may shift liquidity from the OTC market onto the Exchange, which the Exchange believes would increase market transparency as well as enhance price discovery through increased order flow.<sup>44</sup>

The Commission believes this proposal, which permits Micro FLEX Index Options only on broad-based indexes where the value of the underlying is at least 100, strikes a reasonable balance between the Exchange's desire to offer a wider array of investment opportunities and the need to avoid unnecessary proliferation of FLEX options series. However, the Commission

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<sup>40</sup> See Notice, supra note 4, 86 FR at 44416.

<sup>41</sup> See id. In the Notice, the Exchange provided examples of the trading of a Micro FLEX Index Options as compared to a FLEX index option with a multiplier of 100 and the potential benefits for investors. See id. at 44418-19.

<sup>42</sup> See id. at 44416-17.

<sup>43</sup> See id. at 44417.

<sup>44</sup> See id.



expects the Exchange to monitor the trading of Micro FLEX Index Options to evaluate whether any issues develop.

The Commission believes that the proposed rule change is consistent with the Act because it would provide investors with additional investment choices in FLEX options, while also implementing certain protections designed to avoid concerns related to price protections on the non-FLEX market and market fragmentation. In particular, the proposed rule requiring that terms of the Micro FLEX Index Option differ from those of a non-FLEX index option or non-FLEX micro-option can help to address concerns that FLEX options would act as a surrogate for the trading of non-FLEX options.<sup>45</sup> This is important given certain investor protections stated above that exist in the non-FLEX options market that are not present in the FLEX options market.<sup>46</sup> The proposed rule change states that a FLEX index option with an index multiplier of one may not be the same type (put or call) and may not have the same exercise style, expiration date, settlement type, and exercise price as a non-FLEX index option overlying the same index listed for trading (regardless of the index multiplier of the non-FLEX index option).<sup>47</sup> A Micro FLEX Index Option therefore may not have the same terms as a non-FLEX index option or non-FLEX micro-option. This will prevent a Micro FLEX Index Option from being listed with terms identical to those of a non-FLEX index option (with an index multiplier of 1 or 100) on the same index, and is thus designed to avoid price protection and market fragmentation concerns that could arise from trading options with identical terms on the FLEX and non-FLEX markets.

In addition, the Commission believes that the fungibility provisions under CBOE Rule 4.22 will facilitate this change by preventing new Micro FLEX Index Option positions from being opened when a non-FLEX index option with a multiplier of 100 with the same terms is

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<sup>45</sup> See supra note 13 and 16.

<sup>46</sup> See supra note 38.

<sup>47</sup> See proposed CBOE Rule 4.21(b).

listed for trading and by only permitting closing transactions in this situation.<sup>48</sup> Further, pursuant to CBOE Rule 4.22(a), a Micro FLEX Index Option with the same terms as a subsequently added non-FLEX micro-option would become fungible with the non-FLEX micro-option. Accordingly, once a non-FLEX micro-option is added with the same terms as an outstanding Micro FLEX Index Option, the Micro FLEX Index Option would no longer trade in the FLEX options market and instead would become a standardized, non-FLEX option and trade under the same rules that apply to any other standard non-FLEX micro-option.<sup>49</sup>

The Commission also believes that the proposal is consistent with the Act, in particular the protection of investors and the public interest, as it includes several aspects designed to reduce potential investor confusion. In particular, the Commission believes that the proposed treatment of exercise prices, bids and offers, size requirements for FLEX SAM auctions and for crossing orders, and position and exercise limits for Micro FLEX Index Options is consistent with the Act, as these proposed changes should make clear how Micro FLEX Index Options would be quoted and traded<sup>50</sup> and are consistent with the treatment of certain reduced-value index options and micro-options.<sup>51</sup> Additionally, the Commission believes that the use of

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<sup>48</sup> See CBOE Rule 4.22. To facilitate this, the Exchange is providing that if an identical non-FLEX index option with an index multiplier of 100 is added with the same terms as a Micro FLEX Index Option overlying the same index with a multiplier of one, a position established under the FLEX trading procedures may be closed using the trading procedures against another closing only FLEX position during the time period that non-FLEX index option series is listed for trading. See proposed CBOE Rule 4.22(b)(2); see also supra notes 14-16 and accompanying text. In addition, as proposed, CBOE Rule 4.22 would state that the Exchange notifies FLEX Traders when a FLEX options series is restricted to closing only transactions. See proposed CBOE Rule 4.22(b)(2). The Commission believes that permitting such closing only transactions will help investors close out an outstanding Micro FLEX Index Option should a non-FLEX index option with a multiplier of 100 with the same terms subsequently be added.

<sup>49</sup> See CBOE Rule 4.22(a).

<sup>50</sup> The Commission also believes that the examples that the Exchange proposes to add to the rules provide clarity to the operation of the proposed rules. See CBOE Rule 4.21(b)(6) (exercise prices), CBOE Rule 5.3(e)(3) (bids and offers).

<sup>51</sup> The Exchange has made changes to provisions in its rules to reflect that 100 Micro FLEX Index Options will be economically equivalent to one contract for non-FLEX index

different trading symbols for Micro FLEX Index Options should help investors and other market participants to distinguish those options from the related non-FLEX options with a multiplier of 100 and micro-options as well as FLEX index options with a multiplier of 100, reducing potential investor confusion.<sup>52</sup>

The Commission believes it is appropriate for Micro FLEX Index Options to trade pursuant to existing FLEX rules governing the listing and trading of FLEX index options. In addition, the Exchange states that it and OPRA have the necessary systems capacity to handle the additional traffic associated with the listing of new series that may result from the introduction of Micro FLEX Index Options.<sup>53</sup> The Exchange also states that the OCC will be able to accommodate the listing and trading of Micro FLEX Index Options.

As a national securities exchange, the Exchange is required, under Section 6(b)(1) of the Act,<sup>54</sup> to enforce compliance by its members and persons associated with its members with the provisions of the Act, Commission rules and regulations thereunder, and its own rules. The Exchange states that its existing surveillance and reporting safeguards are designed to deter and detect possible manipulative behavior that might arise from listing and trading Micro FLEX Options. In addition, Micro FLEX Index Options will be traded under the Exchange's existing regulatory regime for FLEX index options, which includes, among other things, the Exchange's existing rules regarding customer protection, safeguards related to position and exercise limits, as applicable,<sup>55</sup> and reporting requirements. In particular, Micro FLEX Index Option orders entered by TPHs on behalf of customers, including institutional and retail customers, will be subject to

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option with a multiplier of 100 overlying the same index. See CBOE Rule 5.74 (order size for FLEX SAM), CBOE Rule 5.87 (crossing orders), CBOE Rule 8.35(a)(7) (position limits), CBOE Rule 8.42(g) (exercise limits).

<sup>52</sup> See supra note 11.

<sup>53</sup> See supra note 27.

<sup>54</sup> 15 U.S.C. 78f(b)(1).

<sup>55</sup> There are, however, no position limits or exercise limits for certain broad-based FLEX index options. See CBOE Rule 8.35(b) and CBOE Rule 8.42(g).

all Exchange rules regarding doing business with the public, including those within Chapter 9 of the Exchange's Rules.<sup>56</sup> The Commission believes that it is consistent with the Act to apply Exchange rules governing, among other things, customer accounts, margin requirements, and trading halt procedures to the proposed Micro FLEX Index Options that are otherwise applicable to other FLEX index options. Further, the Commission believes that trading the Micro FLEX Index Options pursuant to the Exchange's current rules governing the trading of FLEX index options is consistent with the protection of investors and should provide market participants with the same flexibility to customize certain terms of the options while allowing investors to trade a smaller sized options contract that may, according to the Exchange, better meet their hedging needs.

The Commission also believes the proposed changes that the Exchange is making regarding codifying how percentage-based FLEX orders and auction responses will be ranked are consistent with the Act.<sup>57</sup> The Exchange states that such ranking provides FLEX Traders willing to pay more (or receive less) with priority.<sup>58</sup> The Exchange further states that providing priority to FLEX Traders that submit more aggressive responses will encourage FLEX Traders to submit competitive responses, which the Exchange believes will benefit investors.<sup>59</sup> In addition,

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<sup>56</sup> The Commission notes that these rules require, among other things, that: (i) a TPH may not accept an option order, including a Micro FLEX Index Option order, from a customer unless that customer's account has been approved for options transactions in accordance with CBOE Rule 9.1; (ii) TPHs that conduct customer business, including institutional and retail customer business, must ensure they provide for appropriate supervisory control over that business and maintain customer records in accordance with CBOE Rule 9.2; and (iii) TPHs will also need to provide customers that trade Micro FLEX Index Option (and any other option) with a copy of the ODD and amendments to the ODD in accordance with CBOE Rule 9.9 so that customers are informed of any risks associated with trading options, including Micro FLEX Index Options.

<sup>57</sup> See proposed amendments to CBOE Rule 4.21(b)(6), CBOE Rule 5.3(e)(3), and CBOE Rule 5.4(c)(4). As discussed above, following the application of the designated percentage to the closing value of the underlying security or index, the system rounds the final transaction prices to the nearest minimum fixed price increment for the class as set forth in Rule 5.4. See CBOE Rule 5.3(e)(3) and CBOE Rule 5.4(c)(4).

<sup>58</sup> See Notice, supra note 4 at 44420.

<sup>59</sup> See id.

the Exchange states that such ranking is consistent with the Exchange's current practice, as well as the way the Exchange ranks dollar-priced premiums.<sup>60</sup> For the foregoing reasons, the Commission believes that the proposed rule change regarding the ranking of percentage-based FLEX orders and options responses is consistent with the Act.

Finally, the Commission believes that the other non-substantive and clarifying changes will help protect investors and the public interest by providing clarity and transparency to the rules by making them easier to read and understand.<sup>61</sup>

Accordingly, the Commission finds that the proposed rule change, as modified by Amendment No. 2, is consistent with Section 6(b)(5) of the Act<sup>62</sup> and the rules and regulations thereunder applicable to a national securities exchange.

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<sup>60</sup> See id. at 44419.

<sup>61</sup> See, e.g., proposed amendments to CBOE Rule 4.21(b)(6) (stating the minimum increments for exercise prices); CBOE Rule 4.22(b) (changing the terminology related to notification of when a FLEX option series is restricted to closing only transactions). See also proposed amendments to CBOE Rule 5.72(c)(3)(A); CBOE Rule 5.73(e); CBOE Rule 5.74(e) (codifying that FLEX auction response bids and offers as well as Initiating Orders and Solicitation Orders with respect to FLEX AIM Auctions and FLEX SAM Auctions, respectively, are ranked during the allocation process based on the dollar and decimal amount of the order or response bid or offer, or the percentage value of the order or response bid or offer, as applicable).

<sup>62</sup> 15 U.S.C. 78f(b)(5).

III. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>63</sup> that the proposed rule change (SR-CBOE-2021-041), as modified by Amendment No. 2, be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>64</sup>

**J. Matthew DeLesDernier,**

*Assistant Secretary.*

[FR Doc. 2021-21211 Filed: 9/29/2021 8:45 am; Publication Date: 9/30/2021]

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<sup>63</sup> 15 U.S.C. 78s(b)(2).

<sup>64</sup> 17 CFR 200.30-3(a)(12).